No. 11947

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

COMMERCIAL WHOLESALERS, INC., a corporation,

Appellant,

vs.

INVESTORS COMMERCIAL CORPORATION,

Appellee.

APPELLANT'S OPENING BRIEF.

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APPELLANT'S OPENING BRIEF.

Commercial Wholesalers, Inc., a corporation, appellant, respectfully submits this its appellant's opening brief upon appeal from the District Court of the United States for the Southern District of California, Central Division.

All italics and underscoring will be supplied unless otherwise noted. Reference to the Transcript of Record will be made by use of the letter "R" followed by appropriate page numbers.

I.

Statement of the Pleadings and Facts Disclosing the Basis Upon Which It Is Contended That the District Court Had Jurisdiction and That This Court Has Jurisdiction Upon Appeal to Review the Judgment in Question.

On December 31, 1946, a petition in involuntary bankruptcy was filed herein against appellant [R. 1-4]. Thereafter appellant filed herein a petition for arrangement under Section 321 in pending bankruptcy, which was filed February 14, 1947 [R. 5-7]. Thereafter, and on May 5, 1947, appellant filed a petition for leave to propose a first amended plan of arrangement under Chapter XI of the Acts of Congress relating to Bankruptcy, together with a first amended plan of arrangement [R. 10-19], and an order herein was granted permitting appellant to propose said modification [R. 9]. Thereafter, and on June 5, 1947, an order was entered herein confirming said arrangement under Chapter XI of the Acts of Congress relating to Bankruptcy [R. 21-25]. On November 12, 1947, a final decree was made and entered herein by the Referee [R. 28-29]. Thereafter, and on December 24, 1947, and pursuant to a petition and order to show cause, said Referee made and entered an order herein modifying said final decree [R. 30-37]. On January 14, 1948, appellant filed herein its petition for review of said Referee's order modifying said final decree [R. 38-46]. On April 2, 1948, the District Court filed its opinion affirming the order of said Referee [R. 58-62] and on April 6, 1948, made and entered its judgment affirming said order [R. 63-64].

Since the principal place of business of appellant at the time of the filing of said petition in involuntary bankruptcy was in the City of Los Angeles, County of Los Angeles,

State of California, it was within the territorial jurisdiction of the United States District Court for the Southern District of California, Central Division. District Courts of the United States are courts of bankruptcy (U. S. C., Title 11, Chapter 1, Section 1, subsection (10)). Courts of bankruptcy are invested with jurisdiction at law and in equity as will enable them to exercise original jurisdiction under the Bankruptcy Act (U. S. C., Title 11, Chapter 2, Section 11). Chapters I-VII of the Bankruptcy Act are incorporated by reference into Chapter XI of the Acts relating to Bankruptcy (11 U. S. C., Section 702). District Courts of the United States have exclusive jurisdiction of a debtor and his property, where the debtor files a petition therein under Chapter XI of the Acts relating to Bankruptcy (11 U. S. C., Section 711). It is therefore respectfully submitted that the District Court had jurisdiction of this matter.

Thereafter, and on May 4, 1948, appellant filed a Notice of Appeal to this Court from the judgment of the District Court affirming said modification of said final decree by the Referee [R. 65-66]. The United States District Court for the Southern District of California, Central Division, is within the territorial jurisdiction of the United States Circuit Court of Appeals for the Ninth Circuit. The Circuit Courts of Appeal of the United States are invested with appellate jurisdiction from the several courts of bankruptcy in their respective jurisdictions in proceedings in bankruptcy, and in controversies arising in proceedings in bankruptcy (U. S. C., Title 11, Chapter 4, Section 27).

From the foregoing pleadings and facts, it is respectfully submitted that said District Court had jurisdiction to enter the judgment appealed from, and that this Honorable United States Circuit Court of Appeals for the Ninth Circuit has jurisdiction on appeal to review said judgment.

II.

Statement of the Case, Together With Questions Involved, and the Manner in Which They Are Raised.

In this case a petition in involuntary bankruptcy was filed against appellant [R. 2-4]. Appellant then filed a petition for arrangement under Section 321 of the Acts of Congress relating to bankruptcy [R. 5-7], said petition was by the United States District Court for the Southern District of California, Central Division, approved, and the matter was referred to Hubert F. Laugharn, Esq., one of the Referees in Bankruptcy of said Court, to take such further proceedings as required by the Acts of Bankruptcy [R. 8]. Thereafter appellant petitioned the District Court for leave to propose a first amended plan of arrangement and filed said plan [R. 10-19] pursuant to an order of said Court [R. 8]. The plan of arrangement provided in part that all unsecured debts of appellant should be settled and satisfied by payment to the holders thereof of forty per cent of their respective claims, with certain provisions attaching thereto [R. 15-16].

Thereafter, and pursuant to application by the debtor [R. 19-20], an order was made and entered herein confirming said plan or arrangement [R. 21-25]. Thereafter, and pursuant to appellant's petition [R. 25-27], a final decree was made and entered by the Referee which among other things ordered, adjudged and decreed that all creditors of appellant whose debts or claims were scheduled or filed should be enjoined and debarred from prosecuting or maintaining any action, suits or proceedings at law or in equity against the debtor or its predecessors [R. 28-29].

Thereafter, the appellee filed and caused to be issued a petition for reconsidering and reforming said final decree and an order to show cause thereon wherein appellee prayed for an order of the Referee reconsidering and reforming the final decree by eliminating and deleting the words "predecessors" therefrom [R. 30-33]. Pursuant to said petition and order to show cause, and on December 24, 1947, the Referee made and entered his order whereby he purported to modify said final decree by striking, deleting and eliminating therefrom the word "predecessors" [R. 34-35].

Thereafter appellant took a review of said Referee's order modifying said final decree to the District Court [R. 38-57]. The District Court thereupon rendered an opinion confirming said order [R. 58-62] and thereafter, pursuant to said opinion, made and entered its judgment wherein it did affirm said order of modification of said final decree made and entered by the Referee on the 24th day of December, 1947 [R. 63].

Thereafter, and on May 4, 1948, appellant filed its Notice of Appeal whereby it did appeal to this Court from said judgment.

The questions involved on this appeal are:

(1) Where a referee has made and entered a final decree or other final order, does the referee thereafter have the power to make or enter an order amending or modifying said final decree, or is that exclusive power vested by law and rule in the United States District Judge to review such final decree?

(2) Where a plan of arrangement under Chapter XI of the Acts of Congress relating to Bankruptcy provides that all of the unsecured debts of the debtor shall be settled and satisfied by the payment of certain amounts set forth in the plan, and the plan is thereafter carried out and the amounts are paid, is there an accord and satisfaction of said debts which acts as a discharge of any obligation of the debtor's predecessor's in interest to pay said obligations?

III.

Specification of Errors.

In accordance with the rules of this Honorable Court appellant hereinafter sets forth its specification of errors relied upon, which are numbered and set out separately.

First Specification of Error.

The judgment appealed from is erroneous for the reason that it affirms an order of the Referee, which order purports to modify a final decree previously made and entered by the Referee, and the Referee had no jurisdiction, power or authority to modify said final decree, all as hereinafter more particularly set forth.

The final decree in this case was made and entered herein on November 18, 1947 [R. 29]. In said final decree the Referee among other things ordered, adjudged and decreed:

> "That all creditors of said Commercial Wholesalers, Inc., a California corporation, Debtor, in the above entitled matter, whose debts or claims against said debtor have been scheduled or filed herein, their heirs, executors, administrators, successors and assigns, be and each of them are hereby forever en-

joined and debarred from pursuing or attempting to pursue, commencing, prosecuting or maintaining any actions, suits or proceedings at law or in equity, against the debtor, its successors, predecessors or assigns, based upon any such debt or claim, scheduled or filed herein, excepting only debts excepted by law from discharge." [R. 29.]

Thereafter appellee filed a petition with the Referee to reconsider and reform said final decree, which was filed November 25, 1947 [R. 30-32]. Pursuant to the appellee's petition, the Referee issued to appellant an order to show cause requiring it to appear and show cause before the Referee on December 4, 1947, why the said final decree should not be reconsidered and reformed in accordance with the prayer of the appellee [R. 33]. The appellee's said petition and the order to show cause came on for hearing on the 4th day of December, 1947, before the Referee, and after hearing the arguments of counsel and taking the matter under consideration, the Referee did, on December 24, 1947, make and enter an order whereby and under the terms of which he purported to modify that portion of said final decree above quoted by eliminating therefrom the word "predecessors," thus causing said quoted portion of said final decree to read as follows:

"That all creditors of said Commercial Wholesalers, Inc., a California corporation, debtor in the above entitled matter, whose debts or claims against said debtor have been scheduled or filed herein, their heirs, executors, administrators, successors and as-

signs be, and each of them are hereby forever enjoined and debarred from pursuing or attempting to pursue, commencing, prosecuting or maintaining any actions, suits or proceedings at law or in equity against the debtor, its successors or assigns, based upon any such debt or claim scheduled or filed herein, excepting only debts excepted by law from discharge." [R. 35.]

No review or appeal of any kind or description was ever taken from the final decree of November 12, 1947, and there were no proceedings of any kind had in this matter from November 12, 1947, to December 24, 1947, save and except as hereinbefore specifically set forth.

SECOND SPECIFICATION OF ERROR.

The judgment appealed from is erroneous for the reason that it affirms an order of the Referee, which order purports to modify a final decree in an arrangement proceeding under Chapter XI of the Bankruptcy Act by eliminating from said final decree an order enjoining unsecured creditors of the debtor from prosecuting or maintaining actions, suits or proceedings against the predecessors of the debtor upon debts or claims scheduled or filed in said proceeding; which is contrary to law for the reason that the debtor's first amended plan of arrangement which was confirmed herein provided that the unsecured debts of the debtor should be settled and satisfied by payment of the amount set forth in the Plan, which amounts were paid, and therefore constituted an accord and satisfaction of said debts and claims, and acted as a discharge of the debtor's predecessors; all as hereinafter more specifically set forth.

The debtor's first amended plan of arrangement which was filed herein provided that the debtor's unsecured claims and debts should be settled and satisfied by payment to the holders thereof of forty per cent of their respective claims [R. 15-16]. This first amended plan of arrangement was confirmed by the Court [R. 21-25] and a final decree entered herein reciting that all the debts of the debtor scheduled herein or upon which claims had been filed had been *fully settled, satisfied, paid and discharged* [R. 28]. Said final decree, among other things, enjoined all of said creditors of the debtor from prosecuting or maintaining any suits or proceedings against the debtor or its predecessors based upon any such debt or claim [R. 29].

Thereafter, and on December 24, 1947, the Referee made and entered an order modifying said final decree by eliminating the word "predecessors" from the final decree [R. 35]. Thus, in effect, refusing to enjoin the creditors whose debts and claims had been "fully settled, satisfied, paid and discharged" [R. 28] from prosecuting said debts or claims against predecessors of the debtor. Since the creditors agreed that their claims should be settled and satisfied by payment to them of forty per cent of their respective claims [R. 15-16], and since the said claims were fully settled, satisfied, paid and discharged [R. 28], the Court erred in entering its judgment affirming the order of said Referee modifying the final decree so as to permit the creditors to maintain actions upon claims which had been paid.

IV.

ARGUMENT.

(1) With Reference to Appellant's First Specification of Error, It Is Respectfully Submitted That the Referee Had No Jurisdiction, Power or Authority to Reconsider, Reform, Modify or Amend Said Final Decree.

The rule in the Circuit Court of Appeals, Ninth Circuit, is well settled that once a Referee has entered an order, the Referee's power over the order is ended. The remedy of review is exclusive, and the Referee may not himself review or change the order.

In re Faerstein, 58 F. (2d) 942.

In the *Faerstein* case cited above, the Referee made and entered a "Turnover Order" and no review thereof was sought. Nine days thereafter the Referee made an order that the turnover order be set aside and annulled. On review, the order setting aside and annulling the turnover order was reversed. On appeal to the Circuit Court, wherein the District Court was affirmed, the Court propounded this question:

> "The issue concisely is, Did the Referee have the power, after having made and entered final findings and conclusions, and after the 'Turnover Order' was issued, to set the same aside, or was the exclusive power vested by law and rule in the United States District Judge to review such order?"

In holding that a Referee had no power to amend his order once it was entered, the Circuit Court said in part:

> "Referees are invested with certain powers, 'subject always to a review by the judge.' Section 66, title

11, U. S. C. A. The referee has no independent judicial authority. He is not a distinct court, and has no power not conferred by order of reference, by law or general orders. 'The district courts of the United States in the several States * * * are made courts of bankruptcy.' 11 U. S. C. A., Section 11. A court is said by Blackstone to be a vested judicial power to adjudicate issues between contending factors, and is composed of the actor, or plaintiff; the *reus,* or defendant; and the *judex,* the judicial power which examines the truth of the contending parties and applies the remedy. A referee is an instrumentality of the Court, with limited powers. His jurisdiction is defined by section 66, title 11, U. S. C. A., *supra,* and his duties are given in section 67. *Neither of these sections gives him the power to review and set aside the order made, and in issue on this appeal.*

"General Order No. 27 of the Supreme Court (11 USCA, Section 53) provides that, when a review is sought of any order of the referee, a petition shall be filed with the referee setting forth the error complained of and the referee shall certify to the United States District Judge the question presented, a summary of the evidence, and finding and the order of the referee thereon. The procedure is specific and clearly stated. Rule 84 of the trial court requires that a petition for review, as provided in General Order 27, *supra,* must be filed with the referee within ten days from the date of notice of such order.

"When an order is entered, the referee's power over the order is ended. The remedy is exclusive and he may not review or change the order. In re Russell (D. C.), 105 F. 501; *In re* Wister & Co. (D. C.), 232 F. 898; also, *In re* Greek Mfg. Co. (D. C.), 164 Fed. 211; *In re* Marks (D. C.), 171 F. 281; *In re* Avoca

Silk Co. (D. C.), 241 F. 607; Matter of J. W. Renshaw's Sons, Bankrupt (D. C.), 3 F. (2d) 75; Matter of Wm. L. David (C. C. A.), 33 F. (2d) 748; David v. Hubbard, 280 U. S. 514, 50 S. Ct. 19, 74 L. Ed. 585.

"That the procedure of review is plainly defined and power limited in the interest of regularity and for the common good is clearly stated by Judge Sawtelle of this court, sitting as District Judge, *In re* Octave Mining Co. (D. C.), 212 Fed. 457, 458, as follows: 'It is manifest that the mode prescribed by General Order 27 is the only manner in which the decisions of the referee may be reviewed. * * *'"

The rule stated in the foregoing case still appears to be the law in this District in view of the fact that it was cited with approval in the later case of

Grandee v. Arizona Wax Paper Co. (C. C. A., 9th Cir.), 90 F. (2d) 801.

(2) With Reference to Appellant's Second Specification of Error, the Order Amending the Final Decree Was Erroneous Because the First Amended Plan of Arrangement and Payment in Accordance Therewith Constituted an Accord and Satisfaction, Extinguishing the Obligations of the Creditor.

The First Amended Plan of Arrangement herein provided that the unsecured debts of the debtor should be settled and satisfied by payment to the holders thereof of forty per cent of their respective claims. Since a Final Decree was admittedly entered herein, reciting that all of the debts of the debtor have been fully *settled, satisfied, paid* and *discharged* [R. 28-29], it cannot be denied but

that the Plan of Arrangement was consummated and the creditors paid their forty per cent of their claims as provided in the Plan. That being true, the original obligations became extinguished by reason of the accord and satisfaction.

An accord is an agreement to accept, in extinction of an obligation, something different from or less than that to which the person agreeing to accept is entitled.

California Civil Code, Sec. 1521.

Though the parties to an accord are bound to execute it, yet it does not extinguish the obligation until it is fully executed.

California Civil Code, Sec. 1522.

Acceptance by the creditors of the consideration of the accord *extinguishes the obligation,* and is called satisfaction.

California Civil Code, Sec. 1523.

In the case of *Russell v. Riley etc.,* 82 Cal. App. 728, at 737, the court said:

> "If the consideration be considered as one of *accord and satisfaction,* then the rule is well settled that where an agreement to accept in full payment a sum less than the amount in dispute is shown to have been fully executed by the payment and acceptance of the lesser sum, *the original obligation is thereby extinguished."*

In the *Estate of Connell,* 121 Cal. App. 703, Mrs. Connell and her deceased husband were jointly liable on an obligation to the plaintiff. Plaintiff filed suit against Mrs. Connell individually (she being administratrix of

her deceased husband's estate) and also filed a claim in the estate for the same obligation. The plaintiff recovered judgment against Mrs. Connell individually, and subsequently accepted from her one-half of the judgment, plus her agreement not to appeal from the judgment, in *payment and satisfaction* of the judgment. Later, plaintiff filed this action against the estate for the balance of the claim. In holding that the accord with Mrs. Connell extinguished the debt and released the estate of Mr. Connell from further payment to the plaintiff, the court said in part:

> "Had the judgment in the civil action been paid in full, appellant could not have recovered anything under the claim filed in the estate. Here we have a situation in which, by accord and satisfaction, the consideration being the payment of one-half of the amount of the judgment on or before the date specified, and the further consideration that the judgment debtor would not prosecute an appeal, the judgment was satisfied, and, by the agreement, the transaction included a settlement not only of the judgment, but of the note and claim in the estate. We hold that, under these conditions, appellant ceased to have any further rights to the recovery of money by reason of the note, and that the settlement extinguished the claims in the estate *as fully as though judgment had been paid in full.*"

In the case of *B & W Engineering Co. v. Bean,* 23 Cal. App. 164, at 170, the court said in part:

> "The phrase 'accord and satisfaction' as it is known and applied in the law means the substitution of a new agreement for and in satisfaction of a preexisting agreement between the same parties. More minutely defined, an agreement of accord and satisfac-

tion is one whereby one of the parties having a right of action against the other, upon a claim arising out of an existing agreement, agrees to accept from the other party something in satisfaction of said right of action different from and usually less than that which might be recovered upon the original obligation (Civil Code, Section 1521). *The effect of such agreement when executed is to extinguish the antecedent liability* (Civil Code, Section 1523)."

In the case of *Keeling Corp., Ltd., v. Pacific Products, Inc.,* 138 Cal. App. 180, the District Court of Appeal held as follows:

"There is a distinction between a discharge in bankruptcy and a composition settlement and the consequences which flow therefrom. A composition with creditors partakes of the nature of a contract, in a measure superseding and outside of the bankruptcy proceedings. It is an offer and acceptance, and the respective rights of the bankrupt and the creditors are fixed by the terms of the offer upon its confirmation. Whether, therefore, a discharge in bankruptcy merely bars the remedy or completely extinguishes the legal obligation is a matter of academic interest, as the composition agreement by its express terms provided the sum paid was 'in full of such creditors' claims' against the corporation. The stockholders were released therefore not by a discharge in bankruptcy but under an express contract. *This agreement completely extinguished and wiped out the entire legal obligation of the company.* It has been universally held that the constitutional liability of stockholders of a corporation for its debts is released by the full performance of a voluntary composition agreement between the corporation and its creditors. (Citing San Jose Savings Bank v. Pharis, 58 Cal. 380.)

"Whatever satisfies or extinguishes the debt as to the corporation, extinguishes also the liability of the stockholders, for the reason that there can be only one satisfaction of the debt (Young v. Rosenbaum, 39 Cal. 646, 654; 6a Cal. Jur. 1018; O'Connell Shoe Co. v. Benson Cooperative Mechanical Co., 175 Minnesota 382). The statutory liability of a stockholder is dependent upon the actual existence of an indebtedness (Ellsworth v. Bradford, 186 Cal. 316). Here, as above indicated, the entire indebtedness has been discharged, satisfied and wiped out. There was, therefore, no debt upon which the alleged statutory liability could be based."

See also to the same effect:

San Jose Savings Bank v. Pharis, 58 Cal. 380, and *Young v. Rosenbaum,* 39 Cal. 646.

V.

Conclusion.

From the foregoing it is respectfully submitted:

(1) That having once made and entered his final decree herein, the Referee had no jurisdiction, power or authority thereafter to reconsider, reform, modify or amend said final decree, and his order of December 24, 1947, purporting so to do was in excess of his jurisdiction; and the judgment of the District Court herein affirming said order is therefore erroneous and should be reversed.

(2) That the Referee's order of December 24, 1947, purporting to modify the final decree herein by deleting the word "predecessors" from the final decree was erroneous because the first amended plan of arrangement providing for the settlement and satisfaction of the debtor's un-

secured obligations by payment of a percentage thereof to its creditors, and the actual payment thereof, constituted an accord and satisfaction between the debtor and its creditors; that the provisions in the final decree prohibiting the creditors from prosecuting actions upon these extinguished liabilities was lawful and proper; and that the judgment appealed from herein is erroneous and contrary to law in so far as the same affirms said Referee's order of December 24, 1947, and for that reason should be reversed.

Respectfully submitted,

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